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C O N F I D E N T I A L MOSCOW 001296

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TAGS: EAGR ECON EINV RS

SUBJECT: UK INFORMALLY PROPOSES G8/RUSSIA FOOD INITIATIVE

REF: MOSCOW 1217

Classified By: Deputy Chief of Mission Daniel A. Russell for reasons 1.
4 (B) and (D)

UK proposal

¶1. (C) During a recent Quad lunch, the British informally floated the idea of a G8 initiative advocating increased production amongst major agricultural economies. The UK Ambassador said his government specifically believes that Russia, historically a grain exporter, could ramp up agricultural production and could play a key role in addressing global supply problems. The UK further believes that a G8 initiative would appeal to Russia's desire to play a greater role in the world and could catalyze Russian action in this regard. The UK Ambassador distributed a non-paper (faxed to EUR/RUS) that spells out this idea in more detail.

Background

¶2. (C) Russia is currently the world's third largest wheat exporter. However, the agricultural sector is operating significantly below production capacity; by some estimates at 60 percent of capacity. Moreover, the immediate challenge for Russia is increasing its agricultural production to meet its own rising domestic demands. Structural problems are significant and investment, while growing, falls short of what is needed. Agricultural Minister Gordeyev has ambitiously called for increasing grain production by 50 percent over the next 12 years. The costs to do so would be billions of dollars: land reclamation would cost between two and five billion dollars; purchasing and modernizing agricultural equipment would cost several billion dollars; and renovating existing capacity also would need investments of several billion dollars annually. Moreover, labor costs are spiraling, as the rural population is rapidly dwindling and labor must be imported from neighboring countries.

¶3. (C) While Gordeyev's goals are theoretically possible, the GOR has not yet developed a comprehensive investment plan of action to increase production. On the contrary, some recent actions adopted by the GOR have removed incentives to increase production. As described in reftel, the GOR

response to high commodity prices has included the imposition of price controls on selected foodstuffs and of export tariffs on grain and fertilizers. Both actions, while designed to control prices, will distort production in the long-term and could drive some agricultural producers out of the market. Russia's membership in the WTO would ameliorate some of the trade and market distortions caused by these policies, another reason to support early accession.

Recommendations

¶4. (C) Post agrees with the UK that active bilateral and multilateral engagement with the Russians on the issue of commodity prices and agricultural production issue would be worthwhile. Bilaterally, we would propose putting the topic of commodity supplies on the agenda of the next meeting of the Economic Dialogue. Multilaterally, we would be in favor of supporting a formal UK call for a G8 initiative. That said, given Russia's supply shortages and the daunting challenges it faces to increase domestic production, we do not believe it will be in a position to help address global commodity imbalances in the short to medium term.

BURNS